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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of)

Inquiry Into Policies and Programs to)
Assure Universal Telephone Service in a)
Competitive Market Environment)

RM-8388

COMMENTS OF BELL ATLANTIC¹

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

I. Introduction and Summary.

Bell Atlantic supports in principle MFS's request for a Commission proceeding to identify the subsidies implicit in existing telecommunications pricing and to determine what subsidies should be prescribed prospectively.² The subsidies that are hidden in existing interstate and intrastate pricing and regulation are incompatible with today's competitive environment and, as the volume of competition increases, will cause the industry to evolve in a manner inconsistent with the dictates of the free market and with the public interest. The investigation MFS seeks is a necessary complement to the rulemaking on access charge reform that USTA has requested and which has drawn

¹ The Bell Atlantic telephone companies ("Bell Atlantic") are The Bell Telephone Company of Pennsylvania, the four Chesapeake and Potomac telephone companies, The Diamond State Telephone Company and New Jersey Bell Telephone Company.

² Petition of MFS Communications Company, Inc. ["MFS"] for a Notice of Inquiry and *En Banc* Hearing (filed Nov. 1, 1993) ("Petition").

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widespread support,³ and the access proceeding should be expeditiously conducted and concluded, even if the universal service investigation is still underway.

While MFS is correct that the system of subsidies to promote universal service, which it calls a "giant fuzzball," causes market and competitive distortions,⁴ MFS vastly oversimplifies the subsidies inherent in the existing regulatory structure. For example, not only are local exchange carriers ("LECs") obligated to serve high-cost areas at below-cost rates, they also must maintain sufficient spare capacity in all areas for redundancy and to meet future service needs, even though those facilities produce no revenue.

LECs must also comply with reams of federal and state regulations, which their competitors largely ignore,⁵ that increase costs and prevent free-market pricing of LEC services. These regulations require the LECs to maintain large staffs of personnel dedicated solely to regulatory support.⁶ The LECs are

³ United States Telephone Association ("USTA"), Reform of Interstate Access Charge Rules, Petition for Rulemaking, (filed Sept. 17, 1993).

⁴ Petition, Att. 1 at 1-2.

⁵ For example, despite clear Commission requirements to file tariffs that specify rates or reasonable ranges of rates, most competitive access providers have refused to revise their non-compliant tariff schedules. See *Tariff Filing Requirements for Nondominant Common Carriers*, 8 FCC Rcd 6752 (1993).

⁶ In some jurisdictions, the LECs must help finance the salaries of the commission members and staff, of consultants, and of "people's counsel" whose principal function is to litigate against the regulated companies.

generally afforded very limited pricing flexibility, and this allows their competitors to umbrella price their services, which seriously distorts the market. This proceeding should determine the nature of these regulatory costs and market distortions and develop a mechanism under which all providers contribute to their recovery.

II. Explicit, Targeted Subsidies Should Replace The Existing System of Implicit, Broad Subsidies.

MFS points out that, in addition to explicit subsidies, the existing interstate pricing system contains an unidentified amount of subsidy designed to support basic local telephone service.⁷ This system of implicit subsidies, which MFS falsely asserts is "perpetuated by the LECs,"⁸ is untenable in a competitive environment.⁹ By artificially increasing the prices for certain services, they provide an uneconomic incentive for competitors, who need not pay the subsidies, to target those overpriced services. As a result, the LECs are placed at a significant competitive disadvantage. As shown below, however, the indirect subsidies and market distortions are far broader than MFS suggests. In a competitive market, all providers should

⁷ Petition, Att. 1 at 1-2.

⁸ *Id.* at 2.

⁹ The system of implicit subsidies long preceded divestiture and was designed in a monopoly environment to keep local rates and rates in high-cost areas lower than costs would otherwise dictate. Unfortunately, as competition developed and grew, subsidies have remained intact.

contribute to all of the costs, direct or indirect, of providing service to the targeted subsidy recipients.

The indirect costs of providing a ubiquitous network must also be taken into account when establishing interconnection charges. MFS apparently does not plan to undertake its own obligation but, instead, to ride to the LECs' coattails through interconnection.¹⁰ The Commission should ensure that the LECs are not forced to subsidize their competitors by absorbing any of the indirect costs of providing the network from which interconnecting providers profit.

The Commission's inquiry should begin by defining those services which public policy requires be universally available.¹¹ Traditionally, the universal service obligation has been restricted to access to basic voice-grade telephone service.¹² Such a restriction may still be appropriate, but the Commission should inquire whether other services should be added based upon current, or anticipated, technological advances and evolving public needs.¹³

¹⁰ See Petition, Att. 1 at 5.

¹¹ See 47 U.S.C. § 151. The National Association of Regulatory Utility Commissioners ("NARUC") is currently investigating the definition of universal service. The Commission should seek advice from NARUC on this issue as both investigations proceed.

¹² See Petition at 10.

¹³ The universal service subsidy should also encompass the costs of such obligations as emergency (911) services where not defrayed by taxes, operator and repair assistance, directory assistance, and white page directories.

Bell Atlantic agrees with MFS that subsidies should be targeted on a need basis.¹⁴ As MFS points out, there is not a necessary correlation between high-cost service areas and the percentage of subscribers that require subsidies in order to afford telephone service.¹⁵ Therefore, it is appropriate to target subsidies on an individual, rather than a geographical basis, to ensure that they fall where absolutely needed to preserve universal basic telephone service.¹⁶ The Commission should inquire, however, into the cost of administering a separate need-based subsidy program and whether existing low-income assistance programs can provide information that could avoid the need for the Commission to certify subsidy recipients. In any event, the general rates in a geographical area should be established at a level that covers all relevant costs.

The Commission should focus on the need for targeted local voice telephone subsidies, then determine the maximum price per line that targeted low-income customers can pay for lifeline telephone service. The difference between that price and the

¹⁴ The Commission should inquire whether the recipients of subsidies should be limited to individuals or whether it should also include certain non-profit institutions such as schools, hospitals, and shelters.

¹⁵ Petition at 10-12.

¹⁶ The amount of the individual customer's subsidy should vary, as it is the difference between the cost of providing service to the customer, including a pro-rated portion of regulation and market distortion costs, less the amount being billed to that customer.

cost of providing service to the customer¹⁷ could be made up through an explicit, broadly-financed subsidy arrangement, as MFS suggests.¹⁸

III. All Implicit Subsidies Need To Be Identified and Quantified.

Besides attempting to quantify the subsidies hidden in the pricing of a variety of interstate and intrastate services, the Commission will need to identify other forms of subsidy that are inherent in the existing disparate regulatory structure.¹⁹ For example, LECs are generally designated as carriers of last resort for a variety of services. Not only must they build capacity to serve current and future universal service requirements, as MFS itself recognizes, but they must construct sufficient spare capacity to serve potential demand.²⁰ This capacity produces no revenue until demand materializes, but it is an obligation which the LECs, and the LECs alone, must bear. Meanwhile, competitors, such as MFS, are free to serve only high-demand areas, where rapid growth quickly turns spare capacity into revenue-producing services. Unless all market participants

¹⁷ The Commission should focus on cost of service to avoid the incentive of a carrier to mark up the price to garner subsidies.

¹⁸ Petition at 19-20.

¹⁹ Subsidies that flow from one intrastate service to another are, of course, subject to state ratemaking jurisdiction.

²⁰ See Petition, Att. 1 at 5.

are willing to shoulder the full range of the LECs' carrier of last resort obligations, they should contribute to the financial burden.

LECs are also subject to intensive regulation at both the federal and state levels, while their competitors enjoy far less stringent regulatory requirements. The cost of this regulation on the LECs is substantial and should be taken into account when calculating the cost of providing service to subsidy recipients. For example, at the federal level, the LECs must cost-justify their tariffs and provide substantial additional information in tariff proceedings.²¹ Their competitors may file tariffs on one day's notice with no justification.²² LECs prepare and file hundreds of pages of detailed, time-consuming reports of various types with the Commission each year, while their competitors have few filing obligations. LECs are subject to frequent detailed audits, while their competitors are rarely if ever audited. These and other regulatory obligations are part of the LECs' costs of providing service, and they should be taken into account when calculating subsidies.

Similarly, the LECs have far less pricing flexibility than their competitors. They are restricted in their right to provide volume and term discounts, to deaverage rates, and to meet marketplace requirements for individual case arrangements. Competitors may market-price all their services and create

²¹ See 47 C.F.R. § 61.38.

²² 47 C.F.R. §§ 61.22-61.23.

individual pricing arrangements to meet specific customers' needs. The restrictions placed on the LECs distort the free market by artificially raising the price of services to some customers, who would receive lower rates under a free-market system. In determining the cost of service for the purpose of calculating the subsidy, the Commission should take into account the price of these market distortions and require all service providers to contribute their share to defray them.

IV. Universal Service Obligations Should Not Favor Any Class of Providers.

Bell Atlantic agrees with MFS that the universal service obligation should be shared equitably among all telecommunications service providers.²³ The method of financing should be designed so that no particular class of providers bears a disproportionate share. Providers such as MFS that target large business and government customers should fully contribute, as should "private" carriers and self-providers. Universal service is a statutory obligation,²⁴ and there is no public interest justification for limiting the burden to any class of customer or provider.

²³ Petition at 19.

²⁴ See 47 U.S.C. § 151.

V. **The Commission Should Initiate An Investigation, But An *En Banc* Hearing Is Unnecessary.**

MFS properly justifies the need for a Commission proceeding on universal service.²⁵ MFS has made no attempt, however, to defend its call for an *en banc* hearing, and one would not be appropriate, at least in this preliminary stage. As shown above, an inquiry into universal service must include an intensive and exhaustive evaluation of current explicit and implicit subsidies, an economic analyses of the need to maintain subsidies to satisfy the statutory requirement for universal service, and an examination of the best manner of spreading the subsidy burden equitably among providers. This type of inquiry is best accomplished through written submissions.

Under these circumstances, an *en banc* hearing would have little value, except to raise the volume of rhetoric by one part of the telecommunications industry against others. Such a political hearing may produce good copy for the press, but it has little role in reasoned decision-making. Accordingly, the Commission should deny, or at least defer, MFS's request for an *en banc* hearing.²⁶

²⁵ Petition at 6-8.

²⁶ The National Telecommunications and Information Administration ("NTIA") has scheduled one public hearing on universal service and has announced plans to hold others. See Announcement on NTIA Bulletin Board (Nov. 29, 1993). The Commission should include the testimony submitted at those hearings into the record of this proceeding.

V. Conclusion.

Accordingly, the Commission should grant MFS's petition in part and initiate an inquiry on universal service. This inquiry should run in parallel with the Commission's rulemaking into access charge reform.

Respectfully submitted,

**The Bell Atlantic Telephone
Companies**

By Their Attorney


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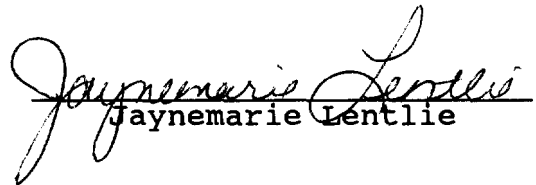
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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing "Comments of Bell Atlantic" was served this 16th day of December, 1993, by first class mail, postage prepaid, on the parties on the attached list.


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